Supreme Court, U.S.
FILED

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No.

IN THE

Supreme Court Of The United States

OCTOBER 1994 TERM

RICHARD MITCHELL and LARRY COTTEN,

Petitioners/Cross-Respondents,

v.

STATE FARM FIRE and CASUALTY COMPANY,

Respondent/Cross-Petitioner.

CROSS PETITION FOR WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

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17 pp

QUESTION PRESENTED

Whether the United States Court of Appeals for the Tenth Circuit erred in vacating the judgments entered in plaintiffs' favor and remanding for a new trial on plaintiffs' breach of duty of good faith and fair dealing claim, rather than reversing and remanding with directions to dismiss plaintiffs' complaint, since plaintiffs did not prove any damages resulting from State Farm's alleged delay in paying their claim.

PARTIES TO THE PROCEEDING

The names of all parties to the proceeding appear in the caption of this cross-petition. Pursuant to Sup. Ct. R. 29.1, cross-petitioner represents that State Farm Mutual Automobile Insurance Company is the parent company of State Farm Fire & Casualty Company.

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Appendix A

Exerpts of Trial Transcript 1a

OPINIONS BELOW

1. *Mitchell v. State Farm Fire & Cas. Co.,* 902 F.2d 790 (10th Cir. 1990).

2. *Mitchell v. State Farm Fire & Cas. Co.,* 15 F.3d 959 (10th Cir. 1994).

3. *Mitchell v. State Farm Fire & Cas. Co.,* 20 F.3d 395 (10th Cir. 1994).

JURISDICTION

The Tenth Circuit issued its opinion vacating the district court's judgments on February 1, 1994. The Tenth Circuit denied petitioners and cross-respondents' petition for rehearing and suggestion for rehearing en banc on April 12, 1994. Cross-respondent is filing this cross-petition for certiorari pursuant to Sup. Ct. R. 12.3. Cross-respondent received petitioners' petition for writ of certiorari on July 13, 1994. This Court retains jurisdiction pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISION

The petition for certiorari purports to implicate the Seventh Amendment to the United States Constitution which states:

> In Suits at common law, where the value in controversy shall exceed $20.00, the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise re-examined in any Court of the United States, than according to the rules of the common law.

STATEMENT OF THE CASE

On September 6, 1976, State Farm issued an insurance policy for fire and extended coverage to Harry H. Hoesli, Jr. and Sarah P. Hoesli of Crested Butte, Colorado as insureds. The policy insured a building located on Castle Road in the town of Mount Crested Butte, Colorado.

On December 2, 1977 the State Farm fire insurance policy insuring this building was assigned to one Michael Pokress.

The building was subsequently purchased by Larry Cotten and Richard Mitchell for $255,000. State Farm consented to the assignment of this policy to Mitchell and Cotten. In connection with the purchase of the property, plaintiffs executed a promissory note to the Pokresses for $130,000. That note was subsequently extended several times.

At the time Mitchell and Cotten requested the assignment of the policy, the policy limit of coverage was $278,300. The policy coverage was increased to $300,000 on January 18, 1983, at the request of Mitchell and Cotten. Mitchell and Cotten requested that State Farm increase the policy limits because their bank, First National Bank of Fort Smith, Arkansas ("the Bank"), required them to do so as they were increasing their mortgage by taking advances on a construction loan on the property. The loan was secured by a second mortgage on the property in the amount of $385,000. The deed of trust on the property which secured the loan to the Bank also required that the insurance be increased to protect the loan.

The policy limits were subsequently increased on two occasions at the request of Mitchell and Cotten. Again, plaintiffs requested State Farm to increase the policy limits because of demands made on them by the Bank as the result of additional funds advanced on the construction loan.

By the time of the arson fire, plaintiffs had taken advances of virtually the entire amount loaned by the Bank and had spent it, but had not done any construction on the property. At the time of the fire, plaintiffs owed approximately $500,000 in loans secured by the property.

On May 27, 1985, the property was totally destroyed by fire. It is undisputed the fire was caused by arson. During the investigation of the claim, State Farm paid the holder of the first mortgage $113,164 in full payment of the note and took an assignment of the note and deed of trust as provided for in the insurance policy. State Farm also paid the insureds for debris removal and demolition under the policy. After the parties failed to reach an agreement as to the amount to which plaintiffs were entitled under the policy and after State Farm invoked the appraisal process, plaintiffs initiated this action in the Western District of Arkansas, Fort Smith Division C, demanding policy limits under the Arkansas valued

policy statute. The case was subsequently transferred to the United State District Court for the District of Colorado pursuant to 28 U.S.C. § 1404(a).

Cross-motions for partial summary judgment were filed by both parties regarding whether Arkansas or Colorado law applied with respect to the amount plaintiffs were entitled to recover under the policy. State Farm's position was that Colorado law applied with respect to the amount of recovery available and that plaintiffs were limited to recovering the actual cash value of the property.

Plaintiffs' position was that Arkansas law applied with respect to the amount of recovery available, and that Arkansas' "valued policy" statute permitted them to recover the policy limits. *See* Ark. Stat. Ann. § 66-3901, now Ark Stat. Ann.§ 23-88-101 (1987).

The district court ruled that Arkansas law applied and that, therefore, plaintiffs were entitled to recover $450,000 rather than the actual cash value of the property. The district court granted the parties' stipulated motion for certification for appeal of interlocutory order pursuant to 28 U.S.C. § 1292(b). The Tenth Circuit Court of Appeals granted State Farm's petition for permission to appeal on June 26, 1989.

The Tenth Circuit reversed the district court's order in *Mitchell v. State Farm Fire & Cas. Co.*, 902 F.2d 790 (10th Cir. 1990) (*"Mitchell I"*) and held that Colorado law applied.

After the Tenth Circuit reversed the district court's decision, and pursuant to the appraisal provision of the insurance policy, the issue as to the additional amount, if any, to which the Bank, as holder of the second mortgage was entitled, was submitted to arbitration. The amount of the second mortgage exceeded the policy limits and therefore no amounts would have been payable to the insureds. The arbitrators made an award based on the actual cash value of the property less amounts paid by State Farm to the holder of the first mortgage, and for debris removal and clean-up, and awarded the Bank $73,268, rather than the policy limits of $450,000 which plaintiffs had demanded. State Farm satisfied the award to the Bank and nothing remained owing to plaintiffs.

Plaintiffs' claims against State Farm for breach of contract and bad faith breach of insurance contract proceeded to trial. The

jury rendered a verdict in State Farm's favor on plaintiffs' breach of insurance contract claim. However, the jury rendered a verdict in plaintiffs' favor on their bad faith breach of insurance contract claim. The jury assessed compensatory damages in the amount of $256,000, the difference between the amount that was paid by State Farm pursuant to the policy, and the policy limits of $450,000.

State Farm then appealed to the Tenth Circuit on several bases, including the contention that it was entitled to judgment as a matter of law since plaintiffs introduced no evidence at trial that they sustained any damages as the result of any of State Farm's conduct. Jurisdiction was based on 28 U.S.C. § 1291.

The Tenth Circuit reversed the district court's entry of judgment in plaintiffs' favor. *Mitchell v. State Farm Fire & Cas. Co.*, 15 F.3d 959 (10th Cir. 1994) (*Mitchell II*). The Court disagreed with State Farm's argument that the jury verdict findings that State Farm did not breach the contract, yet was in bad faith were not irreconcilably inconsistent. 15 F.3d at 962. However, the Court perceived a different inconsistency in the jury's verdicts. The Court held that the jury finding for State Farm on plaintiffs' claim for breach of contract, and then awarding plaintiffs $256,000 on their bad faith claim was inconsistent because no evidence was introduced that plaintiffs sustained $256,000 in damages as the result of any delay in payment of their claim. The Court therefore vacated the judgment entered in plaintiffs' favor and reversed with instructions to retry the bad faith claim. 15 F.3d at 962-963.

Plaintiffs then filed a petition for rehearing and suggestion for rehearing en banc. Plaintiffs argued that the jury's verdicts were not irreconcilably inconsistent because the jury could have awarded them $256,000 in damages based on their "overinsurance" theory of bad faith liability, rather than their "delay" theory of liability.

The Tenth Circuit denied plaintiffs' petition for rehearing and suggestion for rehearing en banc. *Mitchell v. State Farm Fire & Cas. Co.*, 20 F.3d 395 (10th Cir. 1994). The court reasoned that, although plaintiffs alluded to an "overinsurance" theory of liability at trial, the jury was only instructed that plaintiffs could recover on their claim of breach of duty of good faith and fair dealing if it found that State Farm unreasonably delayed payment

of plaintiffs' claim. Because this bad faith instruction directed the jury to a specific theory of liability upon which plaintiffs did not introduce evidence indicating $256,000 in damages, the Court confirmed its initial holding that the jury verdicts were irreconcilably inconsistent.

Plaintiffs filed their petition for certiorari on July 8, 1994. State Farm received plaintiffs' petition for certiorari on July 13, 1994.

REASONS FOR GRANTING THE CROSS-PETITION

A. Plaintiffs did not Prove any Compensable Damages Pursuant to Their Bad Faith Claim

i.

In Colorado, in order to establish a prima facie case of bad faith breach of insurance contract, an insured is required to prove that he sustained damages as the result of the insurer's conduct. Colo. J.I. 25:2 (3d Ed. 1989). Because plaintiffs did not prove that they sustained *any* damages in this case, the Tenth Circuit should have reversed with directions to dismiss plaintiffs' compliant, rather than reaching the issue of whether the jury verdicts were inconsistent.

Generally, an insured who establishes bad faith breach of insurance contract is entitled to recover any economic losses and noneconomic losses caused by the insurer's conduct and which were reasonably within the contemplation of the parties at the time of contracting. *See Farmers Group, Inc. v. Trimble*, 691 P.2d 1138 (Colo. 1984); *Traveler's Ins. Co. v. Savio*, 706 P.2d 1258 (Colo. 1985); *see generally* Shernoff, Gage and Levin, *Insurance Bad Faith Litigation*, § 7.04[1] (1992). For instance, in a first-party bad faith situation in which the insured's apartment burned causing the insured to lose rent monies, recovery of actual damages based on the lost rent value is permissible. *Thico Plan, Inc. v. Ashkouti*, 171 Ga. App. 536, 320 S.E.2d 604 (1984). Where the insured used his tractor to earn a living, lost income from the loss of the use of the tractor would be permitted as consequential damages in a bad faith claim against the tractor's insurer. *Pickett v. Lloyd's*, 252 N.J. Super. 477, 600 A.2d 148 (1991). And, where the plaintiff insured can establish loss of good will and reputation, and loss of profits as

the result of an insurer's bad faith, such items of damages are recoverable. *Drop Anchor Realty v. Hartford Fire Ins. Co.*, 496 A.2d 339 (N.H. 1985).

However, the covenant of good faith and fair dealing neither entitles the insured to payment of claims excluded by the policy nor to anything inconsistent with the limitations contained in the insurance contract, nor to protection in excess of that which is provided for in the contract. *Abdelsamed v. New York Life Ins. Co.*, 857 P.2d 421 (Colo. App. 1992), *rev'd on other grounds*, ___ P.2d ___ (No. 93 SC 3, announced June 20, 1994); *Rawlings v. Apodaca*, 151 Ariz. 149, 726 P.2d 565 (1986).

Plaintiffs introduced no evidence at trial that they sustained economic losses as the result of State Farm's alleged bad faith. They testified to no business loss, no loss of profit, no loss of good will, nor any other economic damages attributable to the purported delay in the payment of their claim for fire loss. It was undisputed that State Farm complied with its contractual obligations to first pay the first and second mortgagees, and since this exhausted the actual cash value, no additional monies were owed to plaintiffs.

The Tenth Circuit stated in its opinion that "[e]vidence of other damage suffered by plaintiffs because of State Farm's delay in making payments to the Pokress family was minimal." 15 F.3d at 962. State Farm submits that such evidence was not "minimal;" it was nonexistent. The only "damage" to which plaintiffs testified was that they did not receive the additional $256,000 representing the difference between the $450,000 policy limit and what was actually owed under the policy. Mr. Mitchell testified that he "assumed" the value of the policy would be paid. (Cross-Pet. App., p.1) His assumption was legally incorrect. *Mitchell I*. The policy specifically stated that benefits would be limited to the actual cash value of the property since plaintiffs did not replace the structure within one year. Mr. Mitchell is presumed to have read and understood the contents of this insurance agreement. *See Atkinson v. Englewood State Bank*, 141 Colo. 436, 348 P.2d 702 (1960). As a matter of law, plaintiffs knew that the policy provided for payment of actual cash value or replacement cost, not policy limits, in the event of destruction.

Essentially, plaintiffs' theory of damages is the same as their "overinsurance" theory of bad faith. As articulated in State Farm's

brief in opposition to plaintiffs' petition for certiorari, this "overinsuring" theory is, under the facts of this case, utterly without merit, if not substantially frivolous. Plaintiffs overinsured their own property in the process of misrepresenting to State Farm and the Bank that they were using construction loan money for its stated purpose. Plaintiffs did not prove, under any legal or logical basis, entitlement to $256,000 in damages.

ii.

A fundamental and long standing principle of judicial restraint requires that courts avoid reaching constitutional questions in advance of the necessity of deciding them. *Lyng v. Northwest Indian Cemetery Protective Ass'n*, 485 U.S. 439, 108 S. Ct. 1319, 99 L.Ed.2d 534 (1988). An appellate court ordinarily avoids reaching a constitutional issue if the case may be resolved on nonconstitutional grounds. *New Kids on the Block v. New America Publishing Co.*, 971 F.2d 302 (9th Cir. 1992); *see also United States v. Smaldone*, 485 F.2d 1333 (10th Cir. 1973).

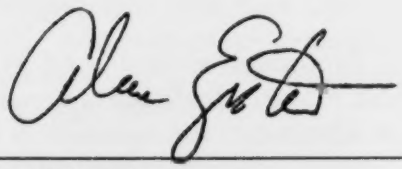
In plaintiffs' petition for certiorari they contend the Tenth Circuit's decision collides with the Seventh Amendment because the jury verdicts could conceivably be reconciled. As set forth in State Farm's brief in opposition to plaintiffs' petition for certiorari, the Tenth Circuit correctly concluded that the jury verdicts were irreconcilably inconsistent. However, a more compelling reason existed upon which the Tenth Circuit could, and should, have predicated its decision. Plaintiffs introduced no evidence that they sustained *any* damages as the result of *any* conduct on the part of State Farm, either in "delaying" their claim or because their property was "overinsured." Therefore, the Tenth Circuit's decision did not go far enough. Because the first element in a bad faith case which an insured must prove is that they sustained damages as the result of any bad faith, the Tenth Circuit should have reversed and remanded with directions to dismiss plaintiffs' complaint. By resolving this issue in State Farm's favor, as State Farm submits the Tenth Circuit should have done, this Court may avoid addressing the constitutional issue raised in plaintiffs' petition for certiorari by affording State Farm the relief it has been entitled to since the conclusion of plaintiffs' case, i.e., dismissal of plaintiffs' complaint.

CONCLUSION

For the foregoing reasons, State Farm requests that this Court grant its petition for certiorari. *See* Sup. Ct. R. 10.1.

Dated this 11th day of August, 1994.

Respectfully submitted,



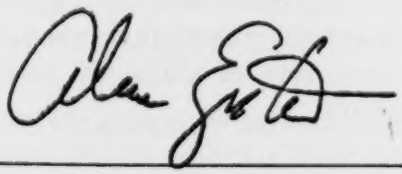
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ATTORNEYS FOR RESPONDENT/CROSS-PETITIONER

CERTIFICATE OF MAILING

I hereby certify that on this 11th day of August, 1994 a true and correct copy of the foregoing **CROSS PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT** was mailed by placing the same in the United States Mail, postage prepaid, addressed as follows:

Miles C. Cortez, Jr., Esq.
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APPENDIX A

Excerpts of Trial Transcript 1a

APPENDIX

Q Now, after you or your attorney received the December 16, 1985, letter from State Farm, you discussed that letter with your attorney and reviewed the replacement bids, market estimate, and decided that those figures were too low for you, right?

A Well, sir, as I've testified, yes, they were very close, we felt. We didn't know any of the contractors. We — I think I had met Mr. Steckel. I think —

Q I'm just asking you: You didn't agree with those? You thought they were too low?

A Yes, sir.

Q And you knew at that time, did you not, Mr. Mitchell, that under your insurance policy, State Farm would pay the replacement cost or policy limits, whichever were less, only if you replaced the building within one year after the fire, right?

A No, I didn't know any such thing, Mr. Hunsaker.

Q You knew that if you didn't replace the building within one year, that the company would only pay actual cash value, did you not?

A I didn't know all of those details, sir. I assumed they would pay the amount of the policy that we'd been paying premiums on all this time.

Q Didn't your attorney, in fact, write to State Farm and ask for additional time beyond the one-year period shortly after